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BEFORE THE

Arizona Corporation Commission

**COMMISSIONERS**

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KRISTIN K. MAYES, Chairman

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PAUL NEWMAN

SANDRA D. KENNEDY

BOB STUMP

AZ CORP COMMISSION  
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IN THE MATTER OF THE REVIEW AND  
POSSIBLE REVISION OF ARIZONA  
UNIVERSAL SERVICE FUND RULES,  
ARTICLE 12 OF THE ARIZONA  
ADMINISTRATIVE CODE

DOCKET NO. RT-00000H-97-0137

IN THE MATTER OF THE INVESTIGATION  
OF THE COST OF TELECOMMUNICATIONS  
ACCESS

DOCKET NO. T-00000D-00-0672

STAFF'S INITIAL POST-HEARING BRIEF

**I. INTRODUCTION.**

In this case, the Arizona Corporation Commission ("ACC" or "Commission") is being asked to establish the appropriate rate levels for intrastate switched access service provided by small Incumbent Local Exchange Carriers ("ILECs") and Competitive Local Exchange Carriers ("CLECs"). Intrastate switched access rates are the rates charged by Local Exchange Carriers ("LECs") to Interexchange Carriers ("IXCs") to access the LECs' network. Intrastate switched access rates make a significant contribution to a carrier's joint and common costs which have helped to keep local rates more affordable in the past.

There are two points on which virtually all parties agree in this case. No one disputes that, in a competitive environment, it makes sense to charge rates that are more reflective of the costs of the underlying service. And, second, most all parties agree that the Commission should undertake access charge reform at this time.

There is less agreement among the parties on the remaining issues in the case. Staff believes that its recommendations reflect sound policy choices on the issues raised as well as an appropriate balance between parties with competing interests in this case. Under Staff's proposal, the small ILEC's and CLECs access charges only would be addressed in this phase of the case. Phase I of the case addressed Qwest's access charges and was consolidated into Qwest's Price Cap Plan Docket; and further charges to Qwest's switched access charges should occur in the Qwest Price Cap Docket.

1 Under Staff's proposal, small ILECs would be required to reduce their access charges to  
2 mirror Qwest's intrastate access rates; unless their interstate rate levels were higher than Qwest's  
3 intrastate access rates. In the latter case, the small ILECs would be required to charge intrastate  
4 switched access rates that mirrored their interstate switched access rates. CLECs would be required  
5 to cap their switched access charges at the ILEC's rates, which closely parallels action taken by the  
6 Federal Communications Commission ("FCC") on this same issue. Under Staff's proposal, ILECs  
7 would be eligible for Arizona Universal Service Fund ("AUSF") support for lost access charge  
8 revenues subject to certain conditions. CLECs would not be eligible for AUSF support for lost  
9 switched access charge revenues because they are not Carriers-of- Last-Resort ("COLR") in the areas  
10 that they serve and thus are not rate regulated to the same extent as the ILECs.

11 Most Arizona Local Exchange Carrier Association ("ALECA") member companies desire to  
12 remain revenue neutral as a result of any switched access rate reductions ordered by the Commission.  
13 While Staff in general does not oppose the concept of revenue neutrality, Staff believes that the  
14 carriers should be required to demonstrate a "need" for any significant increases in rates or for  
15 requests for support from the AUSF. Submission of information contained in a R14-2-103 filing is a  
16 requirement of the current AUSF rules.

17 Carriers always have the option of simply electing to absorb any access charge reductions,  
18 particularly to the extent they are insignificant. Small ILECs should also have the option of proposing  
19 a revenue neutral rate rebalancing plan to make up for the lost switched access charge revenues.  
20 Such rate rebalancing plans would propose increases to the Company's other rates to make up for lost  
21 access charge revenues; without reliance upon the AUSF. Certain financial information would be  
22 required to ensure that the new rates to be charged were just and reasonable under the proposed rate  
23 rebalancing plan. The Commission would have the discretion, however, depending upon the  
24 magnitude of the increases and other factors, to determine whether such plan is appropriate or  
25 whether the Company should be required to submit a rate case filing.

26 Where AUSF support is requested, Staff has presented two alternative proposals. Under  
27 Staff's primary recommendation, before a company would be able to receive AUSF support, the  
28 company would be required to show that it has no other source of funds to offset switched access

1 charge rate reductions. ILECs would be required to file R14-2-103 information to allow the company  
2 and the Commission to increase rates to levels that generate additional revenues while providing  
3 service at reasonable rates, before AUSF funds would be available.

4 Since rate cases can take significant time to process, Staff has put forth an alternative proposal  
5 in the event that the Commission desires to implement access charge reform immediately. Under this  
6 alternative proposal, carriers would be required to file for a waiver of the current rules to receive  
7 temporary AUSF support without having to first go through the rate case process. However, later  
8 these carriers would be required to demonstrate need through a rate case filing to continue to receive  
9 AUSF funding.

10 There are many other important issues raised in this Docket. Staff has structured its brief so  
11 that its position is presented on each of the issues raised in the Commission's October 1, 2009  
12 Procedural Order. Staff's position on all of these issues has been carefully considered and represents  
13 sound policymaking on the issues presented.

## 14 **II. BACKGROUND.**

15 Docket No.T-00000D-00-0672, the "Access Charge Docket," was opened to examine the cost  
16 of access charged by various telecommunications carriers to competitors or other telecommunications  
17 providers for access to their networks. Phase I of the Access Charge Docket addressed Qwest's  
18 ("Qwest") access charges, and was consolidated with and resolved in conjunction with Qwest's rate  
19 cap review. Phase II of the Access Charge Docket was intended to address access charges for all  
20 other Arizona telephone companies that provide switched access services.

21 Docket No. RT-00000H-97-0137, the "Arizona Universal Service Fund" Docket was set up to  
22 review and revise the Arizona Universal Service Fund rules in Article 12 of the Arizona Corporation  
23 Commission rules.

24 The issue of access charges reform is typically addressed in the context of universal service,  
25 particularly in high-cost rural areas. For this reason, the Staff filed a motion to consolidate the  
26 Access Charge and AUSF Dockets which was granted by Procedural Order dated September 19,  
27 2007. The parties were subsequently ordered to file a matrix or list of issues and procedural  
28 recommendations.

1 Issue statements were filed on October 7, 2008 by Cox Arizona Telecom, LLC ("Cox"),  
2 AT&T Communications of the Mountain States, Inc. and TCG Phoenix (collectively "AT&T");  
3 Integra Telecom, Inc. ("Integra"); McLeodUSA Telecommunications Services, Inc.  
4 ("McLeodUSA"); the Arizona Local Exchange Carriers Association ("ALECA"); the Residential  
5 Utility Consumer Office ("RUCO"); Verizon California, Verizon, Business Services, Verizon Long  
6 Distance, and Verizon Wireless (collectively "Verizon"); tw telecom of Arizona LLC ("tw telecom");  
7 XO Communications Services, Inc. ("XO") and the Arizona Payphone Association ("APA").

8 At a January 29, 2009 Procedural Conference, Staff recommended that two workshops be  
9 held. The workshop process was adopted by Procedural Order dated February 3, 2009. A March 17,  
10 2009 Procedural Order determined that Qwest should participate in the process; but sought Staff's  
11 recommendation as to whether changes to Qwest's access charges should be considered as part of  
12 these dockets, or part of Qwest's pending renewal of its Price Cap Plan (Docket No. T-01051B-03-  
13 0454). Staff recommended that Qwest's access charges be addressed in the pending Price Cap Plan  
14 Docket.

15 Workshops were held during the summer of 2009. Parties thereafter submitted further  
16 procedural recommendations. Unable to come to consensus on the issues raised, several of the  
17 parties, including Staff, supported AT&T's request for an evidentiary hearing. By Procedural Order  
18 dated October 1, 2009, it was determined that the following issues would be covered at a minimum:

- 19 1. What carriers should be covered by access reform?
- 20 2. To what target level should access rates be reduced?
- 21 3. What procedures should the Commission implement to achieve the desired  
22 reduction in access rates?
- 23 4. Should carriers be permitted to contract for access rates that differ from their  
24 tariffed rates?
- 25 5. What revenue sources should be made available to carriers to compensate for  
26 the loss of access revenues?

27 ...

- 1                   6.     How much of access cost recovery, if any, should be shifted to end users?
- 2                             What showing should be required for such a shift? What should be the role of
- 3                             “benchmark” rates and how should benchmarks be set?
- 4                   7.     Procedurally, what will be required of a carrier if it seeks a “revenue neutral”
- 5                             increase in local rates?
- 6                   8.     Assuming that AUSF funds will also be used as a compensating revenue
- 7                             source, what specific revisions (including specific recommended amendment
- 8                             language) to the existing rules are needed to allow use of AUSF funds for that
- 9                             purpose?
- 10                  9.     Which carriers should be eligible for AUSF support?
- 11                  10.    What should be supported by AUSF? Access replacement only? High cost
- 12                             loops? Line extensions? Centralized administration and automatic enrollment
- 13                             for Lifeline and Link-up?
- 14                  11.    What should be the basis of AUSF contributions and what should be the
- 15                             structure of any AUSF surcharge(s)?
- 16                  12.    Any other specific revisions to the AUSF rules.

17           The October 1, 2009 Procedural Order also established a procedural schedule, including an  
18 evidentiary hearing. Testimony was filed by the various parties and an evidentiary hearing was held  
19 on March 16-18, 2010. The parties were also ordered to file initial post-hearing briefs and reply  
20 briefs.

### 21 **III. DISCUSSION.**

#### 22 **A. The Record Supports Access Charge Reform this Time.**

23           Most parties agree that intrastate access reform is appropriate at this time for a number of  
24 reasons. Staff Witness Shand identified the following benefits associated with intrastate access  
25 charge reform:

- 26                   1.     Price efficiency.
- 27                   2.     Reduction of arbitrage opportunities.
- 28                   3.     Elimination of differences in rate that occur because of regulatory decisions.

1                   4.       Establishment of more consistent and rational intrastate switched access rates.<sup>1</sup>

2               Several parties point out other benefits associated with switched access charge reform in their  
3 filed testimony in this Docket.<sup>2</sup> In their testimony, Sprint and AT&T discuss the actions taken by  
4 other state commissions to achieve access charge reform; as well as the FCC. Many parties note that  
5 the FCC has a rulemaking planned in the near future to address intercarrier compensation reform on a  
6 comprehensive basis.<sup>3</sup>

7               Only a few parties continue to urge the Commission to proceed cautiously and allow more  
8 time to examine the issues raised<sup>4</sup> or to wait until the FCC acts before proceeding.<sup>5</sup> Staff believes  
9 that the current record provides a good basis for Commission action on the issues of access charge  
10 reform and proposed changes to the AUSF rules addressing access charge reform. While it is true  
11 that the FCC will be initiating comprehensive intercarrier compensation reform in the near future, any  
12 actions taken by this Commission toward reducing access charges as a result of this Docket, are likely  
13 to be consistent with future FCC action.

14               **B.       The Scope of this Case Should Not Be Broadened Beyond Access Charge Reform**  
15               **and Changes to the AUSF Rules Necessary to Accomplish this Reform.**

16               One of the issues raised in the October 1, 2009 Procedural Order was what services should be  
17 supported by AUSF: 1) access replacement, 2) high cost loops, 3) line extensions, 4) centralized  
18 administration and automatic enrollment for Lifeline and Link-up, among others?

19               Staff believes that the issues in this case have been focused upon access charge reform and  
20 revisions to the AUSF necessary to accomplish that reform. In addition, the issue of Lifeline and  
21 Link-up has also been raised and discussed by the parties. However, some other issues have not been  
22 sufficiently vetted in this case. Some parties such as ALECA have proposed broad based changes to  
23 the AUSF rules at this time. For instance, ALECA proposes that the AUSF rules be modified so that  
24 support is based in part on the cost model used to calculate the Federal High-Cost Loop Support.  
25 Issues such as this were not explored enough to provide a sufficient basis for Commission action as

26  
27 <sup>1</sup> Shand Dir. Test., Ex S-1 at 9.

<sup>2</sup> Appleby Dir. Test., Ex. Sprint-1 at 7-8.

<sup>3</sup> Aron Dir. Test., Ex. AT&T-1 at 48-52.

<sup>4</sup> Johnson Dir. Test., Ex. R-1 at 48.

<sup>5</sup> Garrett Dir. Test., Ex. JLEC-1 at 5.

1 this time.<sup>6</sup> Thus, the Commission should limit its rulings at this time to access charge reform; the  
2 proceeding available to carriers to resort to other revenue sources including the AUSF to make up for  
3 lost switched access charge revenues; and the administration of the Lifeline and Link-Up programs.

4 **QUESTION 1: WHAT CARRIERS SHOULD BE COVERED BY ACCESS REFORM?**

5 **A. Access Charge Reform Should Be Targeted to the ALECA Members and CLECS**  
6 **At This Time.**

7 **1. Reform of Qwest's Intrastate Access Charge Rates should continue to be**  
8 **accomplished within the context of its Price Cap Plan.**

9 While many of the IXC's in this Docket believe that Qwest's intrastate switched access rates  
10 should be reduced to mirror its interstate rates, the Commission has already decided that further  
11 reductions to Qwest's access charges should be handled in its Price Cap Plan.<sup>7</sup> This does not mean  
12 that certain policy decisions, for instance how to implement any access charge reductions, could not  
13 be decided for Qwest as well in this Docket. But any decisions regarding the need for further  
14 reductions and the amount of those reductions should be decided within the Price Cap Docket. As a  
15 result of Phase I of the Access Charge Docket, Qwest's switched access rates have already been  
16 reduced by \$27 million annually.<sup>8</sup> Staff does not believe that Qwest's rates should be subject to  
17 further reductions at this time, but rather the focus should be on Phase II of this Docket which would  
18 encompass the remaining ALECA and non-ALECA member small ILECs and the CLECs.<sup>9</sup>

19 **QUESTION 2: TO WHAT TARGET LEVEL SHOULD ACCESS RATES BE**  
20 **REDUCED?**

21 **A. ALECA Member rates should be set at Qwest's intrastate rates or at their**  
22 **interstate levels whichever is higher.**

23 It is Staff's position that access charge reform should target ALECA members and the CLECs  
24 at this time.<sup>10</sup> Unlike Qwest, their intrastate access rates have not yet been reduced, and it is  
25 appropriate at this time to bring their rates more in line with their costs of providing the service.

26 Some parties urge that the transition to interstate levels occur immediately.<sup>11</sup> But, wholesale  
transition to interstate rates for small ILECs at this time would not be in the public interest.

27 <sup>6</sup> Meredith Direct at 13.

<sup>7</sup> October 1, 2009 Proc. Order at 6.

<sup>8</sup> Shand Dir. Test., Ex. S-1 at 3.

<sup>9</sup> *Id.* at 2.

<sup>10</sup> Appleby Dir. Test., Ex. Sprint-1 at 20; Aron Dir. Test., Ex. AT&T-1 at 81.

1 For instance, the testimony of Staff witness Shand indicates that a simple comparison of  
2 interstate per minute access charges with intrastate per minute access charges may be misleading  
3 since it does not take into account the different pricing structures utilized at the federal and state  
4 levels:

5 Interstate access charges are generally lower than intrastate access charges  
6 because of the manner in which costs have been allocated to interstate  
7 access are recovered. Customers currently pay a monthly Subscriber Line  
8 Charge ("SLC") that the FCC instituted when it concluded that non-traffic  
sensitive costs should be recovered through a non-traffic sensitive charge  
rather than through usage-sensitive access charges. No intrastate  
equivalent charge has been implemented by the Commission.<sup>12</sup>

9 So a wholesale transition to interstate per minute access charge levels without more scrutiny  
10 given to the underlying differences in the federal and state pricing structure, is not advisable.

11 In addition, the Commission should remain mindful of the fact that it is dealing with smaller  
12 local exchange carriers which do not have a lot of other jurisdictional sources to make up for the  
13 access charge revenue loss likely to be experienced by a wholesale transition to interstate levels.<sup>13</sup>

14 Finally, the Commission determined in the initial Qwest Price Cap Plan Proceeding, that from  
15 a policy perspective, it made the most sense to phase in access charge reductions over a period of  
16 time.<sup>14</sup> Allowing Qwest to phase in any reductions, but requiring the smaller ILECs to flash cut to  
17 interstate levels, would make little sense. Because of the potential for greater impacts upon their  
18 revenue streams and operations, Phase II should only require smaller ILECs to reduce their access  
19 rates to the higher of Qwest's intrastate access rates or their interstate access rates. The testimony of  
20 Qwest witness Hensley Eckert contains other reasons why a reduction to Qwest's intrastate access  
21 levels is more appropriate at this time.

22 Staff had originally proposed to bring the ALECA member or small ILEC switched access  
23 charge rates down to Qwest's intrastate access charge levels.<sup>15</sup> This was based upon a belief that the  
24 ALECA member individual company interstate access charge rates were lower than Qwest's current  
25

26 <sup>11</sup> Sprint Appleby Direct at 20; AT&T Aron Direct at 81.

27 <sup>12</sup> Shand Dir. Test., Ex S-1 at 4.

<sup>13</sup> Cite to ALECA Testimony and Tr.

28 <sup>14</sup> Cite to Qwest Price Cap Docket.

<sup>15</sup> Shand Dir. Test., Ex. S-1 Exec. Summ. at 2.



1 intrastate access charge rates.<sup>16</sup> However, Staff subsequently discovered through additional discovery  
2 that some carriers' interstate access charge rates are higher than Qwest's intrastate access charge  
3 rates.<sup>17</sup> Staff thus modified its recommendation in the case where an ALECA member's interstate  
4 access charge rates are higher than Qwest's intrastate access charge rates. In that instance, the  
5 ILEC's intrastate rates should be reduced to the level of its interstate access charge rates.<sup>18</sup>

6       **B. CLEC Maximum Access Charges Should be Capped at the Incumbent LEC's**  
7       **Rates.**

8       Staff witness Shand recommends that CLEC maximum switched access rates be capped at the  
9 incumbent LEC's rates,<sup>19</sup> and that the CLECs be required to reduce their maximum tariffed switched  
10 access rates to the level of the ILEC.<sup>20</sup> In this regard, Mr. Shand noted that, "[i]f Staff's access  
11 charge rate reformation is adopted by the Commission, the incumbent LEC's rates will be Qwest's  
12 current intrastate rates."

13       If a CLEC believes that its cost of providing switched access services exceed those of the  
14 ILEC, it should have the option of filing information with the Commission to demonstrate that a  
15 higher maximum rate is appropriate.<sup>21</sup>

16       The approach recommended by Staff witness Shand closely parallels the approach taken by  
17 the FCC when faced with the same issue in its Access Charge Reform proceeding.<sup>22</sup> In that  
18 proceeding, the FCC put a benchmark mechanism in place to limit the potential for CLECs to  
19 inappropriately shift costs to other providers:

20               IXC purchasers of CLEC access services contend that CLECs have  
21               tariffed switched access rates at unjust and unreasonable levels. They  
22               assert that it is an anomaly for a "competitive" provider to enter a market  
23               by charging well in excess of the rate charged by the market's incumbent  
24               and that such entry could not be maintained in a competitive market. The  
25               IXCs argue that high access charges allow CLECs unfairly to shift their  
26               operational expenses and their network build-out expenses to IXCs and, to

27       <sup>16</sup> Shand Rej. Test., Ex.S-5 at 1-2.

28       <sup>17</sup> Shand Rej. Test., Ex.S-5 at 2.

<sup>18</sup> Shand Rej. Test., Ex. S-5 at 2-3.

<sup>19</sup> Shand Dir. Test., Ex. S-1 Exec. Summ. at 2; 11.

<sup>20</sup> *Id.* at 11.

<sup>21</sup> *Id.*

<sup>22</sup> *In the Matter of Access Charge Reform and Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, CC Docket NO. 96-262, Seventh Report and Order and Further Notice of Proposed Rulemaking, (Rel. April 27, 2001). ("FCC CLEC Access Charge Order")

1 long distance ratepayers generally. Moreover, IXC commenters complain  
2 that these unreasonable rates are unilaterally imposed through tariffs,  
rather than negotiation with a willing purchaser. (footnotes omitted).<sup>23</sup>

3 The FCC found that the CLECs should be restricted in the manner that they recover their  
4 costs from access service consumers that have no competitive alternative. The FCC thus  
5 implemented a restriction on the CLEC's exercise of its monopoly power by establishing a  
6 benchmark level at which CLEC access rates will be conclusively presumed to be just and reasonable  
and at (or below) which they may be tariffed.<sup>24</sup>

7 Staff's recommendation actually goes a step further than the FCC's action, by allowing the  
8 CLEC to present information to the Commission which demonstrates that its maximum rate should  
9 be higher due to higher costs of providing service. Staff's proposal is reasonable and should be  
10 adopted.

11  
12 **QUESTION 3: WHAT PROCEDURES SHOULD THE COMMISSISON IMPLEMENT TO**  
13 **ACHIEVE THE DESIRED REDUCTION IN ACCESS RATES?**

14 **A. The Commission Should Order Small ILECs to Reduce Their Access Charges to**  
**Levels Recommended by Staff.**

15 The Commission will initially need to order small ILECs to reduce their access charges to  
16 either the higher of Qwest's intrastate switched access charge rate or the small ILEC's interstate  
17 switched access charge rate. CLECs, on the other hand, would be required to cap their maximum  
18 switched access rates at the ILEC's rates. At the same time, the Commission would need to put in  
19 place procedures to allow for either revenue neutral rate rebalancing if certain conditions are present  
20 or for applications for support from the AUSF, including R14-2-103 information, to make up for lost  
21 switched access charge revenues.

22 **B. There Should be a Demonstration of Need Before AUSF Subsidies are Provided.**

23 Particularly where AUSF monies are being requested, Staff supports a requirement for  
24 carriers to demonstrate "need" for any AUSF funds. Many of the smaller ILECs have not been in for  
25 a rate case in some time. The simple fact that an ILEC may lose \$50 in access revenues, does not  
26 mean that the ILEC needs the whole \$50 repaid in AUSF monies, especially if it is making an  
27

28 <sup>23</sup> FCC CLEC Access Change Order, para. 26.

<sup>24</sup> FCC CLEC Access Change Order, para. 45.

1 excessive rate of return. One must keep in mind that any AUSF surcharge is going to be paid by  
2 customers or end-users statewide. End user customers should not be asked to insulate companies  
3 from competitive losses.

4 Staff witness Shand addressed this issue in his testimony:

5 It is Staff's position that a company should be required to show that it, in  
6 fact, has no other source of funds to offset switched access charge rate  
7 reductions before it is authorized to receive an AUSF surcharge subsidy.  
8 As shown in Exhibit WMS-2, the residential local exchange service rates  
9 for the rural incumbent LECs range from \$9.25 to \$24.46 per month. Staff  
10 believes that it would be inequitable to require ratepayers with a \$24.46  
11 monthly rate to provide an AUSF surcharge subsidy to a company and its  
ratepayers whose monthly local service rate is, for example, \$9.25. Staff  
recommends that the rural incumbent local exchange companies be  
required to file R14-2-103 information to allow the Company and the  
Commission to increase rates to levels that generate additional revenues  
while providing service at reasonable rates, before they are authorized to  
receive AUSF surcharge subsidies.<sup>25</sup>

12 Mr. Shand went on to state that Staff really has no recent sense of the financial condition of  
13 the other ALECA companies other than their assertions that they need AUSF in order to survive the  
14 decline in access revenues. It is not equitable to require customers of other companies to subsidize  
15 the ALECA members based solely on anecdotal statements of need.<sup>26</sup>

16 The ALECA members have taken the position that the Commission  
17 authorized them to charge certain rates and therefore they are entitled to  
18 those revenues in perpetuity. As the Commission well knows, conditions  
19 change, plant depreciates, customer counts change and so forth, so that the  
20 rates approved for these companies may no longer be appropriate.  
21 Further, the FCC has instituted the Multi-Association Group plan that,  
according to the FCC, makes implicit subsidies explicit and also includes  
hold harmless provisions so that rural companies were not harmed  
financially. However, there has been no evaluation of the effects of those  
FCC actions on overall revenue requirements or a determination of  
whether the ALECA members' intrastate rates should be revised.<sup>27</sup>

22 Other parties also support a requirement that small ILECs seeking support from the AUSF for  
23 lost access charge revenues be required to demonstrate a need for any funds received.<sup>28</sup>

24 ...

25 ...

26

27 <sup>25</sup> Shand Dir. Test., Ex. S-1 at 18.

28 <sup>26</sup> *Id.* at 19.

<sup>27</sup> *Id.* at 20-21.

<sup>28</sup> *See, e.g.,* Appleby Dir. Test., Ex. Sprint-1 at 22.

1           **C.     Staff Offered Several Alternatives for Implementing Access Charge Reform**  
2                               **Where AUSF is Requested .**

3                               **1. Staff's Alternative A would incorporate the Current AUSF Rules**  
4                               **Requirement that Carriers file a rate case to demonstrate a need for AUSF**  
5                               **funds.**

6           Staff's primary recommendation is that for a company to receive AUSF support for lost  
7 switched access revenue, the company should be required to show that it, in fact, has no other source  
8 of funds to offset switched access charge rate reductions. The residential local exchange service rates  
9 for small rural ILECs range from \$9.25 to \$24.46 per month. Staff witness Shand pointed out that it  
10 would be inequitable to require ratepayers with a \$24.46 monthly rate to provide an AUSF surcharge  
11 subsidy to a company and its ratepayers whose monthly local service rate is, for example, \$9.25.

12 Thus, under Staff's primary recommendation, the rural ILECs would be required to file R14-2-203  
13 information to allow the Company and the Commission to increase rates to levels that generate  
14 additional revenues while providing service at reasonable rates, before AUSF funds would be made  
15 available.

16                               **2. Staff's Alternative B would allow the Commission to implement a temporary**  
17                               **AUSF surcharge without a full 103 rate case filing.**

18           Staff's Alternative B proposal was designed to allow the Commission to proceed with access  
19 charge reform immediately without first going through a full R14-2-103 process. Under Alternative  
20 B, the Company would be allowed to file an application including financial information sufficient for  
21 the Commission to make a fair value finding and fair value rate of return determination. The  
22 company would also have to demonstrate that the amount of funding requested was revenue neutral  
23 and equal to the amount of lost access charge revenues experienced. The AUSF surcharge would be  
24 interim or temporary in nature. The AUSF surcharge, if approved, would remain in place until the  
25 company's rates had been addressed by the Commission in a rate case.

26           Beginning twelve months after a Commission decision granting the temporary or interim  
27 AUSF support, companies would be required to file a rate case or rate review filing pursuant to  
28 A.A.C. R14-2-103. Staff's recommendation is that such filings take place on a staggered basis due to

1 Staff resource constraints. Staff witness Shand proposed a specific schedule for the ALECA member  
2 filings in his Direct Testimony.<sup>29</sup>

3 **QUESTION 4: SHOULD CARRIERS BE PERMITTED TO CONTRACT FOR**  
4 **ACCESS RATES THAT DIFFER FROM THEIR TARIFFED RATES?**

5 A. Carriers Should Be Permitted to Contract for Access Rates that Differ from  
6 Their Tariffed Rates Subject to Certain Conditions.

7 Qwest raised an issue in this case regarding the appropriateness of contracts between CLECs  
8 and IXC's or others in which the CLEC has given the IXC a rate for switched access service that is  
9 generally lower than its tariffed rate. Staff does not believe that such agreements are inappropriate  
10 where the provider has a provision in its tariff which allows it to do Individual Case Based ("ICB")  
11 Pricing. Staff nonetheless believes that if a company enters into an agreement for switched access  
12 service with an IXC or other provider, the contracts' provisions should be made available to any other  
13 similarly situated customer/carrier which desires to enter into a similar agreement.<sup>30</sup> Staff witness  
14 Shand recommended that if the CLECs enter into these types of agreements, they be required to  
15 amend their tariffs to allow for such contracts and that they also be required to file the agreements  
16 with the Commission for public inspection and that they make the same agreements available to other  
17 similarly situated carriers.

18 **QUESTION 5: WHAT REVENUE SOURCES SHOULD BE MADE AVAILABLE TO**  
19 **CARRIERS TO COMPENSATE FOR THE LOSS OF ACCESS**  
20 **REVENUE?**

21 As discussed, Staff's position is that the small ILEC either choose rate rebalancing or absorb  
22 the cost associated with lost access revenue, if financially possible. The Commission would still have  
23 to review rate rebalancing proposals to determine whether the proposal is acceptable or whether a rate  
24 case would be necessary. For instance, if the magnitude of the amount being requested was  
25 significant, the Commission may desire to proceed through a R14-2-103 filing. The remaining  
26 revenue source would be the AUSF. Staff's alternative proposals with respect to AUSF proceeds  
27 were discussed above.

28 ...

29 *Id.* at 27-28.

30 Copeland Dir. Test., Ex. Q-7 at 4; Oyefus Dir. Test., Ex. AT&T at 55-57.

1 QUESTION 6: HOW MUCH OF ACCESS COST RECOVERY, IF ANY, SHOULD BE  
2 SHIFTED TO END USERS? WHAT SHOWING SHOULD BE  
3 REQUIRED FOR SUCH A SHIFT? WHAT SHOULD BE THE ROLE  
4 "BENCHMARK" RATES AND HOW SHOULD BENCHMARKS BE  
5 SET?

6 **A. The Commission should reject the adoption of a statewide benchmark or national**  
7 **rate as proposed by some Parties.**

8 Several parties to this Docket urge the Commission to adopt a statewide benchmark local  
9 service rate that must be charged before a company is eligible to receive AUSF.<sup>31</sup> For instance,  
10 Qwest proposes that the Commission set a residential benchmark rate at 125% of the statewide  
11 weighted average rates for residential and a business benchmark at 125% of the weighted average  
12 business local exchange rates.<sup>32</sup> AT&T also has a benchmark proposal.<sup>33</sup> Cox proposes the use of a  
13 nationwide benchmark.<sup>34</sup> Under Qwest's proposal, for instance, a local exchange company would  
14 increase its local service rates to the benchmark and then recover any further access revenue losses  
15 from the AUSF.<sup>35</sup>

16 Staff witness Shand urges the Commission to reject the proposals of various parties for the  
17 adoption of a statewide or nationwide benchmark rate for the following reasons:

18 Individual LEC circumstances differ and the Commission should retain its  
19 flexibility to address each company and its ratepayers on an individual  
20 company basis. Current LEC residential local service rates range from  
21 \$9.25 to \$24.46 per month. Qwest's current residential local service rate  
22 is \$13.18 per month. To require the ratepayers of all companies to be  
23 subject to a statewide benchmark rate ignores the disparate cost of  
24 providing service and the different effects the rate increase required might  
25 produce.<sup>36</sup>

26 The use of benchmarks would result in a uniform statewide local service rate which does not  
27 make sense given the diversity of the various telecommunications companies that the Commission  
28 regulates. If the Commission uses benchmarks, it should set a benchmark rate for each individual  
company; rather than a uniform local service benchmark rate for all companies.

29 ...

30 \_\_\_\_\_  
31 Copeland Dir. Test., Ex. Q-7at 4.

32 Oyefusi Dir. Test., Ex. AT&T-7 at 55-57.

33 Garrett Dir. Test., Ex. Cox-1at 10.

34 *Id.*

35 Copeland Dir. Test., Ex. Q-7at 4.

36 Shand Dir. Test., Ex. S-1at 16.

1           **B. IXCs Should Be Required to Pass Through to Their End Users the Access Charge**  
2           **Reductions They Receive As a Result of this Docket.**

3           Staff recommends that IXCs be required to pass through to their end users the access charge  
4 reductions they receive. They should be required to demonstrate that they have done this through a  
5 filing with the Commission which shows that they have passed through the revenue reductions that  
6 occurred as a result of this Docket.<sup>37</sup> This insures that end users will see a concrete benefit from the  
7 reform of access charges.<sup>38</sup>

8           IXCs should also be required to eliminate their Intrastate Connection Charges, to the extent  
9 they have them as well.<sup>39</sup> AT&T has agreed to do so<sup>40</sup> and other IXCs as well.

10           **C. Staff's Proposals in Response to Question 3 Also Address the Issue of How Much**  
11           **Access Cost Recovery Should be Shifted to Ratepayers.**

12           Staff's various proposals for addressing lost access charge revenue addressed in Question 3  
13 also go directly to the issue raised in this Question as to how much access cost recovery should be  
14 shifted to ratepayers.

15           **QUESTION 7:           PROCEDURALLY, WHAT WILL BE REQUIRED OF A CARRIER IF**  
16           **IT SEEKS A 'REVENUE NEUTRAL' INCREASE IN LOCAL RATES?**

17           **A. Staff Believes that Procedures Should be Available to Carriers to Submit a**  
18           **Revenue Neutral Rate Rebalancing Proposal Where They Do Not Seek AUSF**  
19           **Support.**

20           Carriers should have the option of absorbing the access charge reduction, particularly if it is  
21 insignificant. Carriers should also have the option of rate rebalancing on a revenue neutral basis,  
22 without resort to the AUSF. In such a case, Staff recommends that the Company be required to make  
23 a filing with the Commission showing the rate changes it proposes and demonstrating that they are in  
24 fact revenue neutral. The Company would also be required to file financial information sufficient for  
25 the Commission to make a fair value finding and a fair value rate of return finding. The option of  
26 revenue neutral rate rebalancing should only be available where the carriers are not seeking AUSF  
27 support, however.

28           <sup>37</sup> *Id.* at 13.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

1 The Commission in reviewing such an application, would review the magnitude of the  
2 changes being requested and the fair value information to determine whether rate rebalancing was  
3 appropriate or whether a rate case is necessary.

4 **QUESTION 8: ASSUMING THAT AUSF FUNDS WILL ALSO BE USED AS A**  
5 **COMPENSATING REVENUE SOURCE, WHAT SPECIFIC**  
6 **REVISIONS (INCLUDING SPECIFIC RECOMMENDED**  
**AMENDMENT LANGUAGE) TO THE EXISTING RULES ARE**  
**NEEDED TO ALLOW USE OF AUSF FUNDS FOR THAT PURPOSE?**

7 **A. Certain Rule Revisions Would Be Necessary to Implement Staff's Proposed**  
8 **Changes.**

9 Depending upon the course of action chosen by the Commission, certain revisions to the  
10 existing rules may be necessary. The AUSF rules now provide for AUSF funding in high cost rural  
11 areas, but do not specifically permit funding for access charge reform. The rules should be revised to  
12 set forth this new use for AUSF funds and the process for carriers to access AUSF funds for that  
13 purpose.

14 If the Commission decides to adopt the recommendations of the ETCs on Lifeline and Link-  
15 Up, rule changes would also be necessary.

16 **QUESTION 9: WHAT CARRIERS SHOULD BE ELIGIBLE FOR AUSF SUPPORT?**

17 **A. Only ILECs with Carrier-of-Last-Resort Obligations Should be Eligible for AUSF**  
18 **Funds if necessary to Offset Reduced Access Charge Revenue.**

19 ILECs with Carrier-of-Last-Resort Obligations should be eligible for AUSF subsidies if  
20 necessary to offset lost revenues from switched access charge reform. CLECs that are required to  
21 lower their switched access charges as a result of this Docket should not receive lost access charge  
22 revenue through AUSF support. Staff is not aware of any CLEC that is requesting recovery of lost  
23 access charge revenues through the AUSF. Some of the CLEC participants in this Docket even stated  
24 that they would not be seeking AUSF support to offset access charge reform.<sup>41</sup>

25 At least one party has suggested that it may be discriminatory to make the ILECs whole but  
26 not the CLECs, which also experience lost access revenues. Staff disagrees there are several  
27 significant differences between the ILECs and CLECs which would warrant recoupment of lost  
28

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<sup>41</sup> Tr. at 249, 630.



1 switched access revenue by the ILECs but not the CLECs. First and foremost, CLECs have no  
2 Carrier-of-Last-Resort obligation in the areas in which they provide service. Second, the CLECs'  
3 rates are for the most part not set using traditional cost of service principles. Finally, the CLECs  
4 themselves have acknowledged that they should not receive these funds and that disbursement to  
5 them would be inappropriate.<sup>42</sup>

6 **QUESTION 10: WHAT SHOULD BE SUPPORTED BY AUSF? ACCESS**  
7 **REPLACEMENT ONLY? HIGH COST LOOPS? LINE**  
8 **EXTENSIONS? CENTRALIZED ADMINISSTRATION AND**  
9 **AUTOMATIC ENROLLMENT FOR LIFELINE AND LINK-UP?**

10 **A. Staff Recommends Adoption of the Recommendations Contained in the**  
11 **Industry Report on Lifeline and Link-Up.**

12 It is Staff's position that the Arizona Eligible Telecommunications Carriers ("ETCs") be  
13 authorized to implement the recommendations contained in the Report and Recommendations of the  
14 Eligible Telecommunications Carriers on Lifeline and Link-Up Issues ("Industry Report"), docketed  
15 on December 21, 2005. As Staff witness Shand noted in his testimony, in that report, the ETCs  
16 recommended that the Department of Economic Security ("DES") centrally administer the Lifeline  
17 and Link-Up programs of all of the Arizona ETCs. It is anticipated that through this process, as  
18 many as 400,000 new households could be enrolled in Arizona Lifeline over the course of a year, a  
19 substantial increase in today's enrollment levels. It could result in an increase of over \$38 million  
20 dollars in federal funding coming into the state (\$8.00 per month x 12 months x 400,000 households).

21 However, Staff does not recommend that the costs of implementing these recommendations  
22 be recoverable through an AUSF surcharge. The additional revenues received by the ETCs in  
23 conjunction with these new customers, should more than sufficient to cover the costs of  
24 administration. Costs of administration are now covered by the individual carriers and Staff believes  
25 that they should continue to be. There should be no change made with respect to reimbursement of  
26 these costs for ETCs.  
27 ...  
28 ...

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<sup>42</sup> Tr. at 630-31.

1        **B. This Proceeding Should Focus On Access Charge Reform and the Revisions to the**  
2        **AUSF Necessary to Accomplish Access Charge Reform.**

3        Staff does not believe that wholesale revisions to the rules are required at this time. Revisions  
4        to the AUSF should focus upon those necessary to implement access charge reform. Broader based  
5        changes should be considered after the FCC completes its revisions to the federal funding  
6        mechanisms.

7        **QUESTION 11:        WHAT SHOULD BE THE BASIS OF AUSF CONTRIBUTIONS AND**  
8        **WHAT SHOULD BE THE STRUCTURE OF ANY AUSF**  
9        **SURCHARGE(S)?**

10       Another change to the AUSF rules the Commission should consider is to change the basis for  
11       AUSF contributions. Staff witness Shand addressed proposals regarding the way that the current  
12       AUSF surcharges are assessed. Mr. Shand recommends that the AUSF surcharges be assessed on  
13       jurisdictional retail revenues<sup>43</sup> rather than the current methodology which assesses the AUSF  
14       surcharge on intrastate long distance revenues and on interconnection trunks; or the proposals of the  
15       other parties.

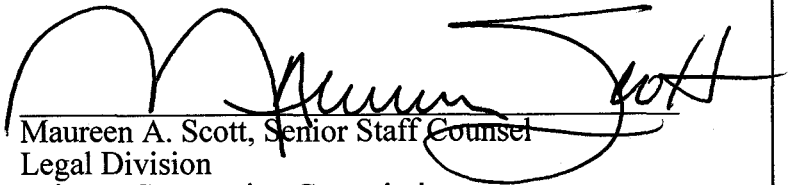
16       **QUESTION 12:        WHAT SPECIFIC REVISIONS TO THE AUSF RULES ARE**  
17       **REQUIRED?**

18       Implementation of Staff's recommendation in response to Question 11 would require a rule  
19       change or amendment.

20       **IV. CONCLUSION.**

21       Staff respectfully requests that the Commission adopt the recommendations of Staff witness  
22       Shand in his testimony filed in this case.

23       RESPECTFULLY SUBMITTED this 9th day of July, 2010.

24         
25       Maureen A. Scott, Senior Staff Counsel  
26       Legal Division  
27       Arizona Corporation Commission  
28       1200 West Washington Street  
      Phoenix, Arizona 85007  
      (602) 542-3402

<sup>43</sup> Accord, Meredith Dir. Test., Ex. ALECA-1at 9.

1 Original and fifteen (15) copies  
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3 9<sup>th</sup> day of July, 2010 with:  
4 Docket Control  
5 Arizona Corporation Commission  
6 1200 West Washington Street  
7 Phoenix, Arizona 85007  
8  
9 Copies of the foregoing mailed this  
10 9<sup>th</sup> day of July 2010 to:  
11 Dan Pozefsky, Chief Counsel  
12 Residential Utility Consumer Office  
13 1110 West Washington, Suite 220  
14 Phoenix, Arizona 85007  
15  
16 Norman Curtright  
17 Reed Peterson  
18 Qwest Corporation  
19 20 East Thomas Road, 16<sup>th</sup> Floor  
20 Phoenix, Arizona 85012  
21  
22 Craig A. Marks  
23 Craig A. Marks, PLC  
24 10645 North Tatum Boulevard  
25 Suite 200-676  
26 Phoenix, Arizona 85028  
27  
28 Michael W. Patten  
Roshka DeWulf & Patten, PLC  
One Arizona Center  
400 East Van Buren, Suite 800  
Phoenix, Arizona 85004  
Mark A. DiNunzio  
Cox Arizona Telcom, LLC  
1550 West Deer Valley Road  
MS DV3-16, Building C  
Phoenix, Arizona 85027  
Jeffrey Crockett  
Bradley S. Carroll  
Snell & Wilmer, LLP  
One Arizona Center  
Phoenix, Arizona 85004  
Arizona Dialtone, Inc.  
Thomas W. Bade, President  
6115 South Kyrene Road, Suite 103  
Tempe, Arizona 85283

Charles H. Carrathers, III  
General Counsel, South Central Region  
Verizon, Inc.  
HQE03H52  
600 Hidden Ridge  
Irving, Texas 75015-2092

OrbitCom, Inc.  
Brad VanLeur, President  
1701 North Louise Avenue  
Sioux Falls, South Dakota 57107

Michael M. Grant  
Gallagher & Kennedy, P.A.  
2575 East Camelback Road  
Phoenix, Arizona 85016-9225

Isabelle Salgado  
AT&T Nevada  
645 East Plumb Lane, B132  
Post Office Box 11010  
Reno, Nevada 89520

Gregory Castle  
AT&T Services, Inc.  
525 Market Street, Room 2022  
San Francisco, California 94105

Thomas Campbell  
Michael Hallam  
Lewis and Roca LLP  
40 North Central Avenue  
Phoenix, Arizona 85004-4429

Arizona Payphone Association  
c/o Gary Joseph  
Sharenet Communications  
4633 West Polk Street  
Phoenix, Arizona 85043

1 Nathan Glazier  
2 Regional Manager  
3 Alltel Communications, Inc.  
4 4805 East Thistle Landing Drive  
5 Phoenix, Arizona 85044

6 Lyndall Nipps  
7 Vice President, Regulatory  
8 Time Warner Telecom  
9 845 Camino Sur  
10 Palm Springs, California 92262

11 Dennis D. Ahlers  
12 Associate General Counsel  
13 Integra Telecom, Inc. &  
14 Eschelon Telecom, Inc.  
15 730 Second Avenue South, Suite 900  
16 Minneapolis, Minnesota 55402

17 Rex Knowles  
18 Executive Director – Regulatory  
19 XO Communications  
20 Suite 1000  
21 111 East Broadway  
22 Salt Lake City, Utah 84111

23 Joan S. Burke, Esq.  
24 Law Office of Joan S. Burke  
25 1650 North First Avenue  
26 Phoenix, Arizona 85012

27 William Haas  
28 McLeodUSA dba PAETEC Business Services  
1 Martha's Way  
Hiawatha, Iowa 52233

Greg L. Rogers  
Senior Corporate Counsel  
Level 3 Communications, LLC  
1025 Eldorado Boulevard  
Broomfield, Colorado 80021

Karen E. Nally  
Law Office of Karen E. Nally, PLLC  
3420 East Shea Boulevard, Suite 200  
Phoenix, Arizona 85028

Scott S. Wakefield  
Ridenour, Hienton & Lewis, PLLC  
201 North Central Avenue, Suite 3300  
Phoenix, Arizona 85004-1052

